**OVERSIGHT BOARD AGENDA STAFF REPORT**

**TO:** Honorable Chair and Members of the Oversight Board

**FROM:** Michael Huntley, Staff liaison from the Successor Agency to the former City of Montebello Community Redevelopment Agency

**SUBJECT:** Update on the State Department of Finance (DOF) action related to the Recognizable Obligation Payment Schedules (ROPS)

**DATE:** June 6, 2012

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## BACKGROUND

On May 2, 2012, the Oversight Board approved ROPS 1 for the period from January 1, 2012 through June 30, 2012 and ROPS 2 for the period from July 1, 2012 through December 31, 2012. Although approved, the Oversight Board questioned a number of line items on the ROPS documents related to the Certificate of Deposits, the reimbursement of the advances made by the City and the allowable administrative charges.

On May 3, 2012, staff forwarded copies of the Board approved ROPS documents via e-mail and ground mail to the County Auditor-Controller, the State Controller and the State Department of Finance.

On May 8, 2012, staff received a call from the DOF. The representative from the DOF informed staff that that ROPS 1 would be denied for a number of reasons, but had still not reviewed ROPS 1 in its entirety. See the attached staff memorandum dated May 8, 2012 with the issues raised over the phone by the DOF.

On May 18, 2012, staff received correspondence from the DOF outlining the line items on ROPS 1 and ROPS 2 that, in the state's opinion, do not qualify as enforceable obligations. See that attached correspondence from the DOF dated May 18, 2012.

On May 24, 2012, the Successor Agency submitted a formal written response to the DOF stating the Agency's legal opinion on those line items the state had indicated were not enforceable obligations. The Successor Agency is waiting for a response from the state. See the attached correspondence from the Successor Agency to the DOF dated May 24, 2012.

On May 25, 2012, staff received correspondence from the DOF stating that the Successor Agency will be receiving its June 1, 2012 property tax allocation, minus the property tax revenue related to those items that the state, in its opinion, do not qualify as enforceable obligations. The DOF also provided an avenue to dispute and amend the ROPS if the Oversight Board disagrees with the state. See that attached correspondence from the DOF dated May 25, 2012.

**DISCUSSION**

As mentioned above, the Successor Agency of the former City of Montebello Community Redevelopment Agency does not agree with the state's opinion on what constitutes an enforceable obligation. The Successor Agency will continue to engage the DOF seeking clarity and/or closure. To date, the Successor Agency has not been contacted by the DOF as to the correspondence sent by the Agency. The Successor Agency anticipates amending ROPS 1 and ROPS 2 to include those items currently denied by the DOF, submitting the amended documents to the Oversight Board for approval and resubmitting those documents to the DOF. Staff will continue to update the Oversight Boards as new information becomes available.

# City of Montebello

Planning and Community Development Department

## Memorandum

DATE: May 8, 2012

TO: Keith M. Breskin, Interim City Administrator
Francesca Schuyler, Director of Finance
Arnold Alvarez-Glasman, City Attorney

FROM: Michael A. Huntley, Director of Planning and Community Development

RE: State Department of Finance – Comments on ROPS 1 approved by the Oversight Board.

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Please be advised that the Veronica Green from the State Department of Finance (SOF) called today to discuss the ROPS 1 documents that were approved by the Oversight Board on Wednesday, May 3, 2012. Ms. Green stated that SOF would be denying ROPS 1 for a number of reasons that will be identified below. The SOF is also directing the Successor Agency to amend the ROPS and provide supporting documents so that she can finish her evaluation of the ROPS documents. Please be advised that staff has already provided most, if not all, of the documents being requested.

**Recognized Obligation Payment Schedule 1**

**Denial:**

Ms. Green identified the following two reasons why ROPS 1 was being denied:

1. **Administrative Fees** – Although the Successor Agency has included an Administrative Transaction Fee line item on ROPS 1, SOF indicated that there are a number of other line items on the ROPS that should have been lumped into the Administrative Fee. Specifically, she is referring to the pension obligation, fiscal agent, project management costs, all attorney fees, and the arbitrage compliance specialist line items. She stated that the cumulative total of the line items mentioned above plus the Administrative Transaction Fee would put the Successor Agency over the administrative allotment and as such, SOF is denying ROPS 1.
2. **Certificate of Participation and Advances** – SOF indicated that they do not believe that the Certificate of Participation and the Advances are recognizable obligations and should be removed from the ROPS.

**SOF request for supporting documents or changes to ROPS 1:**

Page 1:

1. Line Item No. 9 Certificate of Participation – Requesting supporting documentation.
2. Line Item No. 10 Montebello Hills Housing Deferral – Requesting supporting documentation and an improved description of the obligation on the ROPS.
3. Line Item No. 11 SERAF Repayment – Requesting supporting documentation and an improved description of the obligation on the ROPS.
4. Line Item No. 12 Repayment on Advances – Requesting supporting documentation and an improved description of the obligation on the ROPS. Also, she specifically stated that if this item is left on the ROPS, SOF will continue to disapprove ROPS 1.
5. Line Item No. 13 through 18 – SOF has indicated that all five of these line items should have been included in the Administrative Budget for the Successor Agency. Since these line items are considered by the State as administrative items, inclusion of these items into the proposed Administrative Budget would cause the Successor Agency to be over the allotted Administrative Budget and as such, the SOF is denying ROPS 1.

Page 2:

1. Line Item No. 5 needs to be included in the Administrative Fee.

Page 3:

1. Line Item No. 4 Certificate of Participation – Requesting supporting documentation.
2. Line Item No. 5 SERAF Repayment – Requesting supporting documentation and an improved description of the obligation on the ROPS.
3. Line Item No. 6 Repayment on Advances – Requesting supporting documentation and an improved description of the obligation on the ROPS. Also, she specifically stated that if this item is left on the ROPS, SOF will continue to disapprove ROPS 1.
4. Line Item No. 7 through 11 – SOF has indicated that all five of these line items should have been included in the Administrative Budget for the Successor Agency.

Page 4:

1. Line Item No. 3 needs to be included in the Administrative Fee.

Page 5:

1. Line Item No. 4 SERAF Repayment – Requesting supporting documentation and an improved description of the obligation on the ROPS.

2. Line Item No. 5 Repayment on Advances – Requesting supporting documentation and an improved description of the obligation on the ROPS. Also, she specifically stated that if this item is left on the ROPS, SOF will continue to disapprove ROPS 1.
3. Line Item No. 6 through 11 – SOF has indicated that all five of these line items should have been included in the Administrative Budget for the Successor Agency.
4. Line Item No. 8 Fiscal Agent - The Finance Department needs to address the terms in the indenture agreement with SOF.

Page 6:

1. Line Item No. 3, 607 W. Whittier Blvd. – Requesting supporting documentation.
2. Line Item No. 4-8, Advances - Requesting supporting documentation.

**General Comments from SOF**

1. SOF is requesting that all Administrative Fees be included on a separate sheet and in the same format as the ROPS document.

2. Management from the SOF has identified those items that are considered administrative fees including:

    a. Contracts for payroll
    b. Audit services
    c. Successor Agency pay
    d. Oversight Board pay
    e. Property management fees
    f. All legal fees include litigation
    g. Office supplies
    h. Lease for successor Agency office space
    i. Insurance
    j. Utilities

    Fees that may have been considered administrative but can be added to the ROPS include:

    a. Appraisal costs
    b. Closing costs

3. SOF has directed that all items on the ROPS that do not have payments due during the six month period be removed from the ROPS.

4. SOF has stated that the ROPS will be denied if there are any blanks on the ROPS, if the descriptions are poorly written and if items are left on the ROPS that SOF has requested be removed.

5. ROPS 2 will have to be amended based on the direction by SOF on ROPS 1.

6. Since SOF has directed that changes be made to the both ROPS documents, the Oversight Board will have to review and approve both of the documents before they are forwarded back to the state.

DEPARTMENT OF FINANCE

EDMUND G. BROWN JR. • GOVERNOR

915 L STREET ■ SACRAMENTO CA ■ 95814-3706 ■ WWW.DOF.CA.GOV

May 18, 2012

Michael A. Huntley, Director of Planning and Community Development
City of Montebello
1600 West Beverly Boulevard
Montebello, CA 90640-3932

Dear Mr. Huntley:

Pursuant to Health and Safety Code (HSC) section 34177 (l) (2) (C), the Montebello Successor Agency submitted a Recognized Obligation Payment Schedule (ROPS) to the California Department of Finance (Finance) on May 3, 2012 for the periods January through June 2012 and July through December 2012. Finance staff contacted you for clarification of items listed in the ROPS.

HSC section 34171 (d) lists enforceable obligation (EO) characteristics. Based on a sample of line items reviewed and application of the law, the following do not qualify as EOs:

January through June 2012 ROPS:

- Project Montebello Hills, Page 1, items 9 and 12; Project South Montebello Industrial, page 3, items 4 and 6; and Project Montebello Economic Revitalization, page 5, item 5 – Certificates of Participation (COP) and advances totaling $10.5 million. No documentation was provided that pledge tax increment as the source of funding for the COP. HSC section 34171 (d) (2) states that agreements, contracts, or arrangements between the city, county, or city and county that created the redevelopment agency and the former redevelopment agency are not enforceable obligations.

- Project Montebello Hills, page 1, item 10 – Montebello Hills Housing Deferral in the amount of $6.5 million for 20 percent housing set aside. The requirement to set aside 20 percent of RDA tax increment for low and moderate income housing purposes ended with the passing of the redevelopment dissolution legislation. HSC section 34177 (d) requires that all unencumbered balances in the Low and Moderate Income Housing Fund be remitted to the county auditor controller for distribution to the taxing entities.

- Administrative cost claimed exceeds allowance by $172,202. HSC section 34171 (b) limits fiscal year 2011-12 administrative expenses to five percent of property tax allocated to the successor agency or $250,000, whichever is greater. Five percent of the property tax allocated is $330,521; therefore, $172,202 of the claimed $502,723 is not an enforceable obligation. The following line items were considered administrative costs:

| Page | Item No. | Project Name | Amount |
|---|---|---|---|
| 1 | 13 | Administrative Transaction Fee | $197,563 |
| 1 | 17 | Attorney's Fees | 75,000 |
| 1 | 18 | Arbitrage Compliance Specialist | 625 |
| 3 | 7 | Administrative Transaction Fee | 77,783 |
| 3 | 11 | Attorney's Fees | 45,000 |
| 3 | 12 | Arbitrage Compliance Specialist | 375 |
| 5 | 6 | Administrative Transaction Fee | 76,127 |
| 5 | 10 | Attorney's Fees | 30,000 |
| 5 | 11 | Arbitrage Compliance Specialist | 250 |
| | | **Total:** | **$502,723** |

July through December 2012 ROPS:

- Project Montebello Hills, Page 1, items 9 and 12; Project South Montebello Industrial, page 3, item 4; and Project Montebello Economic Revitalization, page 5, item 5 - Certificates of Participation and advances totaling $3.4 million. HSC section 34171 (d) (2) states that agreements, contracts, or arrangements between the city, county, or city and county that created the redevelopment agency and the former redevelopment agency are not enforceable obligations.

- Administrative cost claimed exceeds allowance by $381,425. HSC section 34171 (b) limits fiscal year 2012-13 administrative expenses to three percent of property tax allocated to the successor agency or $250,000, whichever is greater. Three percent of the property tax allocated is $99,580; therefore, the administrative cost allowance is $250,000. The following line items were considered administrative costs:

| Page | Item No. | Project Name | Amount |
|---|---|---|---|
| 1 | 13 | Administrative Transaction Fee | $163,500 |
| 1 | 14 | Pension Obligation | 4,782 |
| 1 | 17 | Attorney's Fees | 142,835 |
| 2 | 5 | Audit Fees | 15,000 |
| 3 | 7 | Administrative Transaction Fee | 55,500 |
| 3 | 8 | Pension Obligation | 2,869 |
| 3 | 11 | Attorney's Fees | 85,701 |
| 3 | 12 | Arbitrage Compliance Specialist | 375 |
| 4 | 3 | Audit Fees | 9,000 |
| 5 | 6 | Administrative Transaction Fee | 32,400 |
| 5 | 7 | Pension Obligation | 1,913 |
| 5 | 10 | Attorney's Fees | 107,500 |
| 5 | 11 | Compliance Specialist | 4,050 |
| 6 | 10 | Audit Fees | 6,000 |
| | | **Total:** | **$631,425** |

As authorized by HSC section 34179 (h), Finance is returning your ROPS for your reconsideration. This action will cause the specific ROPS items noted above to be ineffective until Finance approval. Furthermore, items listed on future ROPS will be subject to review and may be denied as EOs.

If you believe we have reached this conclusion in error, please provide further evidence that the items questioned above meet the definition of an EO and submit to the following email address:

Redevelopment_Administration@dof.ca.gov

Finance may continue to review items on the ROPS in addition to those mentioned above and identify additional issues. We will provide separate notice if we are requesting further modifications to the ROPS. It is our intent to provide an approval notice with regard to each ROPS prior to the June 1 property tax distribution date.

Please direct inquiries to Evelyn Suess, Supervisor or Michael Barr, Lead Analyst at (916) 322-2985.

Sincerely,

Mark Hill

MARK HILL
Program Budget Manager

cc: Ms. Kristina Burns, Program Specialist III, Los Angeles County Auditor Controller

City of Montebello

May 24, 2012

**VIA E-MIAL <Redevelopment Adminitration@dof.ca.gov>**

Mark Hill, Program Budget Manager
California State Department of Finance
915 L Street
Sacramento, CA 95814

Re: Department of Finance Comments on Montebello ROPS

Dear Mr. Hill:

Successor Agency the City of Montebello ("**Successor Agency**") is in receipt of the Department of Finance's ("**DOF**") May 18, 2012 letter, in which DOF objects to several items included on the Successor Agency's draft Recognized Obligations Payment Schedule ("**ROPS**").

Please allow the following to serve as the Successor Agency's initial, formal written response to DOF's objections.

## CERTIFICATES OF PARTICIPATION ARE PROPERLY LISTED ON THE ROPS

The Successor Agency disputes DOF's position that the Certificates of Participation ("**COP's**") identified on the draft ROPS do not qualify as "enforceable obligations."[1]

The COPs relate to the financing of certain public facility improvement projects (the "**Projects**") of benefit to the Montebello Hills and South Industrial project areas (the "**Project Areas**"), under which third-party investors provided funds for the Projects in return for the promise of a future revenue stream. The COP's were first issued in 1990, pursuant lease agreements ("**Lease Agreements**") between the City and the Montebello Public Improvement Corporation ("**MPIC**"), a nonprofit public benefit corporation organized under California's Nonprofit Public Benefit Corporation Law for the purpose of establishing the legal and financial mechanism for issuance of COP's.[2] The COP's constituted an undivided fractional interest in the right to receive lease payments by the City, and were marketed and purchased by private third party investors through an underwriter hired by the City as part of the overall 1990 COP issuance (the "**1990 COP Issuance**").

[1] The COPs challenged by DOF are: Project Montebello Hills, page 1, item 9, and Project South Montebello Industrial, page 3, item 4.

[2] The MPIC was incorporated on April 18, 1990 and is comprised of a Board of Directors identical to the membership of the Montebello City Council (*i.e.*, each sitting City Council member holds a corresponding position as Board member of the MPIC), with the City's Mayor serving as MPIC's President, the City Clerk serving as its Secretary, *etc.*

Critically, the financial structure of the 1990 COP Issuance included agreements between the City and the Community Redevelopment Agency of the City of Montebello (the "**Agency**") whereby the Agency pledged to pay the City's lease payment obligations (the "**1990 Reimbursement Agreements**"). Such pledge constituted payment for the redevelopment benefits provided by facilities financed by the COP's which specifically benefited the Project Areas. Under the Reimbursement Agreements, the City's lease payment obligations were paid from a portion of the Agency's tax increment revenue stream from the Project Areas. Thus, thirdparty investors who purchased Certificates pursuant to the 1990 COP Issuance essentially acquired interests in a portion of the tax increment revenue stream of the Project Areas, as guaranteed by the 1990 Reimbursement Agreements. The 1990 Reimbursement Agreements were thus clearly "indebtedness obligations," as such term is defined in ABx1 26.[3]

As the Lease Agreements were amended and restated throughout the 1990's,[4] the 1990 Reimbursement Agreements were likewise replaced by corresponding new Reimbursement Agreements, preserving an identical financial structure whereby the Project Area's tax increment revenue stream covered the City's payments under the Lease Agreements which, in turn, were paid to third party investors who purchased Certificates. The most-recent of these Reimbursement Agreements are those entered-into in connection with the Second Amended and Restated Lease Agreement entered-into in 2000 (the "**2000 COP Issuance**").

The Reimbursement Agreements reflected at page 1, line 9, and page 3, line 4 of the Successor Agency's ROPS are a part of that 2000 COP Issuance. These Reimbursement Agreements (the "**2000 Reimbursement Agreements**") likewise reflect the Project Area's obligations to pledge tax increment revenues toward the City's obligations under the Second Amended and Restated Lease Agreement – ***obligations which are paid to third party investors who purchased Certificates from the 2000 COP Issuance, establishing a direct thirdparty interest in the 2000 Reimbursement Agreements, themselves***.

Indeed, as with prior COP Issuances, the 2000 COP Issuance includes a purchase contract between the City and an underwriter, Seidler-Fitzgerald Public Finance (the "**Underwriter**"), for the Underwriter's purchase of $22,930,000 Series 2000 Certificates, and marketing and sale of the same to third party investors (the "**2000 COP Underwriter Agreement**"). The 2000 COP Underwriter Agreement specifically references the 2000 Reimbursement Agreements and obligates the City and Agency to perform the 2000 Reimbursement Agreements as assurance to the Underwriter that sufficient revenues will be available to cover the City's lease payments under the Second Amended and Restated Lease Agreement. The Underwriter Agreement provides:

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[3] Health & Safety Code § 34171(d)(3).

[4] The 1990 COP Issuance was supplemented by a subsequent COP issuance in 1992 (corresponding to new facilities lease agreements), a 1993 COP issuance (corresponding to a First Amended and Restated Lease Agreement), and a 2000 COP issuance (corresponding to a Second Amended and Restated Lease Agreement). Each such issuance included corresponding Reimbursement Agreements between the City and Agency preserving the financial structure described above.

> "[The City represents and warrants to the Underwriter that ... the City is a public body duly organized and existing under and by virtue of the laws of the State of California and has all necessary power and authority to adopt the resolutions authorizing, among other things ... ***the South Montebello Reimbursement Agreement, [and] the Montebello Hills Reimbursement Agreement***...." (2000 COP Underwriter Agreement, § 4(1) [emphasis added].)

Thus, under the Underwriter Agreement, the City represented and warranted the validity and binding effect of the 2000 Reimbursement Agreements. Moreover, Section 6 of the Underwriter Agreement provides that the Underwriter expressly undertakes its obligations "***in reliance on, and ... subject to, the due performance by the City ... of the covenants and agreements to be observed and performed hereunder***" (emphasis added), and specifically indicates that the "Legal Documents" – which include the 2000 Reimbursement Agreements[5] – are valid, binding, and effective upon the parties:

> "The Underwriter's obligations under this Purchase Contract are and shall be subject, at the option of the Underwriter, to the following further conditions as of the Closing: [¶] at the time of the Closing, ***the Legal Documents*** [*i.e.*, the 2000 Reimbursement Agreements and other applicable documents] ... shall be ***in full force and effect as valid and binding agreements between the various parties thereto*** and the Legal Documents ... shall not have been amended, modified or supplemented except as may have been agreed to in writing by the Underwriter...."[6]

Thus, the 2000 Reimbursement Agreements not only function as an interest held by third party investors who purchased Certificates from the 2000 COP Issuance, but also function as a binding contractual revenue source securing the Underwriter's rights under the 2000 COP Underwriter Agreement.

Moreover, under the 2000 COP Issuance (and all prior COP Issuances), the Agency's tax increment revenues are paid not to the City, but directly to the trustee overseeing and managing the COP's: pursuant to Section 2 of the Reimbursement Agreements, the Agency makes lease payments directly to the trustee, BNY Western Trust Company, who holds such funds in trust for third party investors who have interests in the lease payments pursuant to their Certificates. Thus, third party investors who purchased Certificates pursuant to the 2000 COP Issuance have effectively invested in the Project under the premise – and in reliance thereon – that the future revenue stream flowing under the COP's would be provided by the Agency.

Based upon this, the challenged COP's fall squarely within the bounds of Health & Safety Code § 34171(d)(1)(E), which ***includes*** within the definition of "enforceable obligation" all "legally binding and enforceable agreement or contract that is not otherwise void as violating the debt

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[5] Pursuant to Section 4(1) of the Underwriter Agreement, "Legal Documents" include the "Trust Agreement, this Purchase Contract, the Lease Agreement, the Site Lease, ***the South Montebello Reimbursement Agreement***, ***the Montebello Hills Reimbursement Agreement***, the Escrow Deposit and Trust Agreement and Continuing Disclosure Certificate." Underwriter Agreement §4(1) (emphasis added).

[6] Underwriter Agreement § 6(1).

limit or public policy." The challenged COP's were executed in 2000 and evidence their investment in the Projects, and entitle them to a specific revenue stream. In this case, the pledged revenue stream was the lease payments made by the Agency under the Reimbursement Agreements. In fact, the holders of the COP's have been receiving regular payments flowing from the Agency's satisfaction of the Lease Agreement obligations since 5/1/2001.

Indeed, although Health & Safety Code § 34171(d)(2) excludes certain agreements between cities and their redevelopment agencies from the definition of "enforceable obligations," this subdivision ***expressly*** recognizes certificates of participation – such as those presently challenged by DOF – as "enforceable obligations." Namely, § 34171(d)(2) provides that agreements executed to secure or repay "indebtedness obligations" are "enforceable obligations":

> "[W]ritten agreements entered into (A) at the time of issuance, but in no event later than December 31, 2010, of ***indebtedness obligations***, and (B) solely for the purpose of securing or repaying those indebtedness obligations may be deemed ***enforceable obligations*** for the purposes of this part." (Emphasis added.)

Critically, the definition of "indebtedness obligations" provided in Health & Safety Code § 34171(d)(3) specifically includes "certificates of participation" within its scope:

> "'Indebtedness obligations' means...***certificates of participation***...***issued*** or delivered by the redevelopment agency, or a joint powers authority created by the redevelopment agency, ***to third-party investors or bondholders to finance or refinance redevelopment projects***..." (Emphasis added.)

The purpose of including "indebtedness obligations" within the scope of an "enforceable obligation" was ***to ensure that the investments of third parties are <u>not</u> destroyed by the implementation of ABx1 26***.[7] With regard to the 2000 Reimbursement Agreements, it is undisputed that these Agreements were entered-into in connection with the 2000 COP Issuance which provides third party investors who purchased Certificates a direct interest in the tax increment revenue paid pursuant to the 2000 Reimbursement Agreements. Additionally, revenue provided pursuant to the 2000 Reimbursement Agreements is a contractual obligation to the Underwriter pursuant to the 2000 COP Underwriter Agreement, and a revenue source paid directly to the trustee under the 2000 COP Issuance, BNY Western Trust Company. ***Not recognizing the COP's and Reimbursement Agreements as "enforceable obligations" on the Successor Agency's ROPS will destroy the existing investments and revenue streams of these parties, directly in contradiction to the mandates of ABx1 26.***

Indeed, the COP's and Reimbursement Agreements not only fall under the scope of the quoted authority above, but also constitute "indebtedness obligations" by virtue of their "evidenc[ing

[7] *See, e.g.*, Health & Safety Code § 34175(a) ("[T]he cessation of any redevelopment agency shall not affect either the pledge, the legal existence of that pledge, ***or the stream of revenues available*** to meet that pledge." (Emphasis added.)

indebtedness, issued or delivered by the [Agency], to third-party investors," pursuant to additional terms at Health & Safety Code § 34171(d)(3).

Given this, the COP's and 2000 Reimbursement Agreements qualify as "enforceable obligations" meeting the requirements of Health & Safety Code § 34171(d)(2); that is "indebtedness obligations" that were (A) entered into at the time of issuance, and (B) have a sole purpose of securing repayment. Unquestionably, the challenged COPs satisfy this standard: the COPs were issued to secure third-party investments in a public redevelopment-related project, and which guarantee the investors' right to a future stream of revenue generated by the Agency's lease payments.

Moreover, though this point is clear based upon the foregoing, it must be emphasized that the COP's and interests in the 2000 Reimbursement Agreements are ***investor-owned securities***, the default of which would raise severe negative consequences for third-parties and therefore run afoul of the Legislative intent underling ABx1 26. In adopting ABx1 26, the Legislature made clear its intention ***not*** to impair private third-party investments or to place at risk the interests of third-party bondholders relying on redevelopment-related financial instruments. This intention is made clear, for example, by Health & Safety Code § 34171(d)(1)(A), which expressly defines "enforceable obligations" as "[b]onds..., including the required debt service, reserve set-asides and any other payments required under the indenture or similar documents governing the issuance of the outstanding bonds of the redevelopment agency."

To remove any doubt on this point, the Legislature expressly announced its intention to safeguard the interests of private third-party investors in Health & Safety Code § 34175(a):

> "It is the intent of this part that pledges of revenues associated with enforceable obligations of the former redevelopment agencies are to be honored. It is intended that the cessation of any redevelopment agency ***shall not affect either the pledge, the legal existence of that pledge, or the stream of revenues available to meet that pledge***." (Emphasis added.)

Interpreting ABx1 26 so as to ***remove*** the COP's and Reimbursement Agreements from the ROPS would run counter to the entire Legislative framework of ABx1 26, and would expose third party investors to substantial financial risk. Importantly, the revenue stream flowing to the third party investors who purchased Certificates pursuant to the 2000 COP Issuance was guaranteed by the Agency via the 2000 Reimbursement Agreements, and third party investors, Underwriter, and trustee invested in the COP's based upon this assumption. In the event DOF removes the COP's from the ROPS, the obligation to satisfy the COP revenue stream will be shifted to the City. This result would frustrate the purpose of the COP investment, substantially reduce – if not completely dissolve – the value of the investment, and completely thwart the expressed legislative intent of ABx1 26; to protect third-party investors. Indeed, ***this result would unconstitutionally impair the third-party investors' contractual rights under the COP's and Reimbursement Agreements***.[8]

[8] *See* U.S. Const. Art. I, § 10; Cal. Const. Art. I, § 9; *Fourth La Costa Condominium Owners Ass'n v. Seith* (2008) 159 Cal.App.4th 299 (obligations of contract are unconstitutionally impaired by a law which renders them invalid, ore releases or extinguishes them); *Goodman v. Riverside County* (1983) 190 Cal.App.3d 900

Nevertheless, DOF's position appears to require this result, as it seeks removal of the COP's and Reimbursement Agreements from the Successor Agency's ROPS, thereby shifting repayment obligations to the City's general fund which, importantly, is already running at an estimated $3 million deficit for fiscal year 2012-2013. As such, the City is unlikely to be able to satisfy its former Agency's obligations to the COP holders, likely resulting in their default.

The Successor Agency does not believe that DOF intends to cause defaults on the COP's, and certainly ABx1 26 does not provide for this. Accordingly, and in consideration of the foregoing, the Successor Agency strongly disputes DOF's position concerning removal of the COP's from the ROPS, and believe that position should be seriously reconsidered.

**REPAYMENT OF ADVANCES ARE PROPERTLY LISTED ON THE ROPS**

The Successor Agency also disputes DOF's position that certain "repayment on advances" (the "**Repayment Advances**") should not be included on the ROPS.[9]

The Advances are related to a formal agreement, dated 1979, entered into between the City and the Agency, whereby the Agency contracted with the City for the provision of administrative and contractual services and facilities required to operate the Agency, (hereinafter simply the "**Agreement**"), as is authorized by Health & Safety Code §§ 33126 and 33128. The Agreement formalized an administrative policy under the same terms, dated 1976. The Advances included on the ROPS represent outstanding amounts owed the City by the Agency under the Agreement.

It is unquestionable that the Agreement constitutes a valid, enforceable contract. The Agreement was executed pursuant to express statutory authority granted redevelopment agencies under the Health & Safety Code and, having been in place and performed by the City and Agency for over thirty (30) years, DOF – along with any other public agency – is estopped from challenging their validity.[10]

Indeed the Agreements date back to the origin of the Agency's project areas, and therefore arguably qualify under Health & Safety Code § 34171(d)(2), as a loan agreement entered into between the City and Agency within two years of the Agency's creation. Namely, the Agency's project areas were not created until 1973 (South Montebello Industrial Redevelopment Project Area), 1975 (Montebello Hills Redevelopment Project Area), and 1982 (Montebello Economic Revitalization Project Area), respectively. Because, under the former Community Redevelopment Law, redevelopment agencies were not authorized to act absent identification

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(unconstitutional impairment of contractual obligations may arise when only portion of bondholder's security has been removed).

[9] DOF challenges: Project South Montebello Industrial, page 3, item 6; Project Montebello Economic Revitalization, page 5, item 5.

[10] Under California's validation statutes, failure to challenge validity of city contract, or adoption of a redevelopment plan, beyond 60 days of its approval impliedly validates it, preventing a retroactive challenge by any interested parties, including third-party state agencies. (CCP § 863, *City of Ontario v. Superior Court* (1970) 2 Cal.3d 335; *Millbrae School Dist. v. Superior Court* (1989) 209 Cal.App.3d 1494)

of project areas and pursuant to a formalized redevelopment plan, the Agency's creation date is irrevocably linked to the formation of the its project areas. Accordingly, because the Agreement was formalized in 1979, and the administrative policy had been in place since 1976, the Advances relate to the "creation period" of the Agency, and therefore should be recognized as "enforceable obligations" pursuant to Health & Safety Code § 34171(d)(2).

Based upon the foregoing, and pursuant to related constitutional and equitable principles that require satisfaction of the obligations owed the City under the Agreements, the Successor Agency disputes DOF's determination that the Repayment Advances do not qualify as an enforceable obligation, and insist they be included on the ROPS.

**SUCCESSOR AGENCY "ADMINISTRATE ATTORNEY'S FEES" AND FEES INCURRED IN ENFORCING RDA RIGHTS ARE SEPARATE ITEMS ON THE ROPS**

The Successor Agency also disputes DOFs position that several items listed on the ROPS constitute administrative costs, as opposed to separate "enforceable obligations," and therefore the Successor Agency has exceeded its administrative cost allowance.

In particular, the Successor Agency disagrees with DOF's position that all attorney's fees incurred by the Successor Agency are administrative in nature, as the vast majority of legal costs were necessary incurred by the Successor Agency in ongoing lawsuits involving the former redevelopment agency, and in preserving the former agency's interest in pending redevelopment projects. Such expenses are better characterized as "project-related," and are therefore properly included as a separate "enforceable obligation" on the ROPS.

Specifically as to the Successor Agency, for example, the majority of legal fees listed on the ROPS arise from an ongoing lawsuit, *Sevacherian, et al. v. Redevelopment Agency of the City of Montebello, et al.* (Los Angeles County Superior Court Case No. BC 437787) (hereinafter the "***Sevacherian* Action**"), wherein the Successor Agency is defending claims that the former redevelopment agency is in breach of a real estate purchase agreement. This litigation should be familiar to DOF because it, along with the Oversight Board, and the county and State auditor-controllers, have been named as individual parties in the action, and will soon be forced to defend it in their individual capacities.

Defending the *Sevacherian* Action, or any other ligation involving the former agency, has nothing to do with the ***administrative*** operations of the Successor Agency. Rather, retaining and paying legal counsel to enforce the former Agency's rights – ***as ABx1 26 requires*** – is properly characterized as a separate "enforceable obligation" under Health & Safety Code § 34171(d)(1)(E) as a "legally binding and enforceable agreement or contract that is not otherwise void as violating the debt limit or public policy."

The same is true for legal costs incurred in connection with pending redevelopment projects. Health & Safety Code § 34177(c) requires the Successor Agency to "[p]erform obligations required pursuant to any enforceable obligation." Unquestionably, this includes performance of development agreements that pre-date ABx1 26, and which necessarily require the retention of legal counsel to ensure the transaction is performed in accordance with legal requirements, and in a manner preserving the former agency's interest. Again, these costs are associated with

"legally binding and enforceable contracts"[11] and therefore fall squarely within the scope of "enforceable obligations" – ***not administrative costs***.

Indeed, Health & Safety Code § 34171 defines the "Administrative Budget" as "the budget for ***administrative costs of the Successor Agency*** as provided in Section 34177," and Health & Safety Code § 34177(j)(1) similarly describes the administrative budget as including "[e]stimated amounts for ***Successor Agency administrative costs*** for the upcoming six-month fiscal period." (Emphasis added.) Use of the qualifying term "***administrative*** costs," rather than merely "costs," is critical in discerning the Legislature's intent. Namely, by limiting the "costs" to be included in the Administrative Budget as only those that are "administrative" in nature," the Legislature envisioned that all other "non-administrative" costs would be outside the scope of a Successor Agency's Administrative Budget.

Interpreting ABx1 26 otherwise would be legally faulty, and would run afoul of the foundational principle of statutory interpretation: *expressio unius est exclusio alterius* ("the expression of certain things in a statute necessarily involves exclusion of other things not expressed....").[12] In other words, by expressly limiting the Successor Agency's Administrative Budget to "administrative" costs, it must be implied that other "non-administrative" costs which otherwise qualify as "enforceable obligations" need ***not*** be confined to the Administrative Budget, but rather listed as separate independent qualifying obligations on the ROPS.

We further note that ABx1 26 ***expressly contemplates*** a separation of certain costs incurred by the Successor Agency. In that vein, ABx1 26 includes within its definition of "enforceable obligations" "contracts or agreements necessary for the administration or operation of the Successor Agency, in accordance with this part, including but not limited to, agreements to purchase or rent office space, equipment and supplies, and pay-related expenses..."[13] Such contracts are not included in "administrative costs," but rather are included as an "enforceable obligation" to be included on the ROPS as a separate item. Attorneys' fees incurred in ongoing redevelopment related matters should similarly be considered separate "enforceable obligations," as such costs are necessary to accomplish the objectives of ABx1 26, as opposed to its day-to-day administrative operations as a Successor Agency.

On this point, the Successor Agency directs DOF to Exhibit 4 of its own Q & A's concerning ABx1 26, available on DOF's website, which provides that "***employees working on specific [redevelopment] project implementation activities such as construction inspection, project management, or actual construction would not be viewed by Finance as 'administrative.'***" (Emphasis added.) Thus in its own guidelines, DOF considers "ongoing" project related costs as separate from administrative costs, and there is no reason this rational should not extend to expenses incurred in ongoing litigation concerning redevelopment matters.

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[11] Health & Safety Code § 34171(d)(1)(E)

[12] *Dyna–Med, Inc. v. Fair Employment & Housing Comm'n* (1987) 43 Cal.3d 1379, 1391 at note 13; *see also People v. Gray* (2011) 199 Cal.App.4th Supp. 10, 15 ("The Legislature's failure to do so requires us to apply the principle of *expressio unius est exclusio alterius*, that is, that 'the expression of one thing in a statute ordinarily implies the exclusion of other things.'" [*quoting In re J.W.* (2002) 29 Cal.4th 200, 209]).

[13] Health & Safety Code § 34171(F).

Finally logically, it makes little sense to include legal fees incurred in ongoing redevelopment matters agency in the finite – and relatively small – administrative budget. The costs of legal fees incurred in ongoing redevelopment matters alone will likely exceed, or at least substantially deplete, the limited $250,000 budget allocated for administrative expenses. This is not what the Legislature intended in ABx1 26, nor is it what the law provides.

The Successor Agency requests that DOF recalculate the Successor Agency's administrative costs pursuant to the foregoing.

**ARBITRAGE COMPLIANCE AND FISCAL AGENT FEE'S SHOULD NOT BE INCLUDED IN THE SUCCESSOR AGENCY'S ADMINISTRATIVE BUDGET**

In addition to DOF's improper inclusion of attorneys' fees, the Successor Agency also disputes DOF's inclusion of the cost of "arbitrage compliance specialists" and "fiscal agent fees" in its administrative cost calculation.

Like the attorneys' fees discussed above, the cost of arbitrage compliance specialists and fiscal agent fees were necessarily incurred by the former Agency in connection with bonds issued to fund redevelopment projects, and the cost incurred by the Successor Agency in maintaining and evaluating those bonds moving forward is irrevocably tied to such projects. Thus such costs are "project related," as opposed to "administrative," and were properly included by the Successor Agency as a separate enforceable obligation on the ROPS.

Again, the Successor Agency directs DOF to its own guidelines, which provide that "employees working on specific [redevelopment] project implementation activities such as construction inspection, project management, or actual construction would not be viewed by Finance as 'administrative.'" Specialists necessarily retained by the former Agency, and now the Successor Agency, qualify within this directive.

Given the foregoing, the Successor Agency requests that DOF reconsider including arbitrage compliance specialists and fiscal agent fees in its "administrative costs" calculation.

**OVERSIGHT BOARD LEGAL FEES SHOULD NOT BE INCLUDED IN THE SUCCESSOR AGENCY'S ADMINISTRATIVE BUDGET**

Finally, the Successor Agency disputes any position by the DOF which requires the Successor Agency to pay for the costs and/or fees of legal counsel retained by the Oversight Board. Again, Health & Safety Code § 34171 defines the Successor Agency's "Administrative Budget" as "the budget for administrative costs ***of the Successor Agency***...." (Emphasis added.) Health & Safety Code § 34177(j)(1) similarly describes the administrative budget as including "[e]stimated amounts for ***Successor Agency*** administrative costs for the upcoming six-month fiscal period." Nothing in ABx1 26 requires or authorizes successor agencies to pay the legal fees that Oversight Boards, themselves, incur. Indeed, ABx1 26 omits, entirely, any reference to the administrative costs incurred by Oversight Boards in its description of the

administrative budget.[14] At a minimum, this omission evidences an intention to exclude the Oversight Board's legal costs as a responsibility of the Successor Agency.

This is an issue of critical importance to the Montebello Oversight Board because, as noted above, it has been ***named*** and ***served*** as a ***separate independent defendant*** in the *Sevacherian* Action. As such, the Oversight Board will presumably need to retain independent legal counsel to defend itself in this litigation, and ***the costs for such legal counsel go far beyond the costs which the Successor Agency is obligated to pay for under ABx1 26***.[15]

Furthermore, by expressly including the costs of Oversight Board meetings as an administrative budget allowance, and expressly omitting ***any other costs*** of the Oversight Board from the being included, the legislature clearly intended that the latter not be included. In short, nothing in ABx1 26 authorizes Oversight Boards to determine the staffing of a Successor Agency's employees – including attorneys – nor does it include such costs in the administrative budget of the Successor Agency.

**THE DOCUMENTATION REQUESTED BY DOF HAS ALREADY BEEN PROVIDED**

We note that DOF's May 18, 2012 letter states that no documentation was provided in support of several of the ROPS items submitted by the Successor Agency to DOF. This is not an accurate statement, as such documentation has previously been provided to DOF in prior distributions from the Successor Agency. In an effort to establish a clear record of this, we respectfully note the following:

- Staff of the Successor Agency have recently been in contact with staff at DOF who have addressed this issue.

- Specifically, in these recent communications the DOF staff members have stated that the request for documentation has been stated as "boilerplate" language inserted into all letters of the DOF submitted to various successor agencies throughout the State and this language was not intended to apply to the Montebello Successor Agency, *per se*.

- DOF staff have expressed their belief that the request for documentation submitted to the Montebello Successor Agency in the DOF's May 18, 2012 was made based on such "boilerplate" language and does not actually reflect the state of the Successor Agency's submission of documentation in support of its ROPS.

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[14] Health & Safety Code § 34179(c) provides that "[t]he Successor Agency shall pay for all of the costs of ***meetings of the Oversight Board***" (emphasis added), but does ***not*** require the Successor Agency to pay the Oversight Board's separate costs for legal counsel. Rather, at most, this Section requires successor agencies to pay for the Oversight Board to have an attorney present at its meetings.

[15] *See*, note 5, *supra*. The legal defense of the Oversight Board in litigation is something that neither ABx1 26, Health & Safety Code § 34179(c), nor any other legal authority requires the Successor Agency to pay for.

- Accordingly, it is the Successor Agency's understanding that all required documents have been provided and further documentation is not presently requested by DOF.

Notwithstanding the foregoing, to the extent DOF wishes for the Successor Agency to re-submit any or all of the documents already provided, or needs additional documentation supporting the Successor Agency's position, the Successor Agency is more than willing to provide it. Please contact the undersigned for any requests in this regard.

**CONCLUDING REMARKS**

In closing, to the extent the DOF disputes the position taken by the Successor Agency on any of the matters discussed above, the Successor Agency requests that DOF specifically identify their objections clearly and in writing, so that the Successor Agency may properly record, digest and, if necessary, respond to DOF's position.

Very truly yours,

Francesca Tucker-Schuyler
Interim City Administrator/Interim Executive Director
City of Montebello/Montebello Successor Agency

cc: Evelyn Suess, Supervisor, DOF
Michael Barr, Lead Analyst, DOF

DEPARTMENT OF FINANCE

EDMUND G. BROWN JR. • GOVERNOR

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May 25, 2012

Michael A. Huntley, Director of Planning and Community Development
City of Montebello
1600 West Beverly Boulevard
Montebello, CA 90640-3932

Dear Mr. Huntley:

Subject: Recognized Obligation Payment Schedule Approval Letter

Pursuant to Health and Safety Code (HSC) section 34177 (l) (2) (C), the Montebello Successor Agency submitted Recognized Obligation Payment Schedules (ROPS) to the California Department of Finance (Finance) on May 3, 2012 for the periods of January to June 2012 and July to December 2012. Finance is assuming appropriate oversight board approval. Finance has completed its review of your ROPS, which may have included obtaining clarification for various items.

Except for items disallowed in whole or in part as enforceable obligations noted in Finance's letter dated May 18, 2012, Department of Finance is approving the remaining items listed in your ROPS for both periods. This is our determination with respect to any items funded from the Redevelopment Property Tax Trust Fund (RPPTF) for the June 1, 2012 property tax allocations. If your oversight board disagrees with our determination with respect to any items not funded with property tax, any future resolution of the disputed issue may be accommodated by amending the ROPS for the appropriate time period. Items not questioned during this review are subject to a subsequent review, if they are included on a future ROPS. If an item included on a future ROPS is not an enforceable obligation, Finance reserves the right to remove that item from the future ROPS, even if it was not removed from the preceding ROPS.

Please refer to Exhibit 12 at http://www.dof.ca.gov/assembly_bills_26-27/view.php for the amount of RPTTF that was approved by Finance based on the schedule submitted.

As you are aware the amount of available RPTTF is the same as the property tax increment that was available prior to ABx1 26. This amount is not and never was an unlimited funding source. Therefore as a practical matter, the ability to fund the items on the ROPS with property tax is limited to the amount of funding available in the RPTTF.

Please direct inquiries to Evelyn Suess, Supervisor or Michael Barr, Lead Analyst at (916) 322-2985.

Sincerely,

Mark Hill

MARK HILL
Program Budget Manager

cc: Ms. Kristina Burns, Program Specialist III, Los Angeles County Auditor Controller